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OCT 13 1927
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Nos. 554 and 555

In the Supreme Court of the United States

OCTOBER TERM, 1927

ELIZABETH C. TAFT, PETITIONER

v.

FRANK K. BOWERS, COLLECTOR OF INTERNAL REVENUE FOR THE SECOND DISTRICT OF NEW YORK

GILBERT C. GREENWAY, JR., PETITIONER

v.

FRANK K. BOWERS, COLLECTOR OF INTERNAL REVENUE FOR THE SECOND DISTRICT OF NEW YORK

ON PETITIONS FOR WRITS OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

MEMORANDUM FOR THE RESPONDENT

U. S. GOVERNMENT PRINTING OFFICE: 1927

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In the Supreme Court of the United States

OCTOBER TERM, 1927

No. 554

ELIZABETH C. TAFT, PETITIONER

v.

FRANK K. BOWERS, COLLECTOR OF INTERNAL REVENUE for the Second District of New York

No. 575

GILBERT C. GREENWAY, JR., PETITIONER

v.

FRANK K. BOWERS, COLLECTOR OF INTERNAL REVENUE for the Second District of New York

ON PETITIONS FOR WRITS OF CERTIOARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT.

MEMORANDUM FOR THE RESPONDENT

OPINIONS BELOW

The District Court for the Southern District of New York disposed of both of these cases in one opinion (*Taft case*, R. 13; *Greenway case*, R. 20) which is reported in 15 F. (2d) 890. The Circuit Court of Appeals for the Second Circuit also de-

cided the cases together, each of the three judges, however, writing separate opinions, one dissenting (*Taft case,* R. 27; *Greenway case,* R. 33). These opinions are reported in 20 F. (2d) 561.

JURISDICTION

The judgments sought to be reviewed were entered in each case July 13, 1927. (*Taft case,* R. 44; *Greenway case,* R. 50.) Petition for certiorari was filed in the *Taft case* September 26, 1927, and in the *Greenway case* October 3, 1927. Jurisdiction is conferred upon this Court by Section 240(a) of the Judicial Code as amended by the Act of February 13, 1925.

QUESTION PRESENTED

Both cases present the single question whether or not Section 202(a)(2) of the Revenue Act of 1921, which requires the donee upon the sale of property acquired by gift after December 31, 1920, to use the cost of the property to the donor as the basis for computing profit, is constitutional in so far as it taxes as income to the donee the appreciation in the value of the gift prior to its acquisition by the donee.

THE STATUTES

Section 202(a)(2) of the Revenue Act of 1921, c. 136, 42 Stat. 227, 229, provides:

> That the basis for ascertaining the gain derived or loss sustained from a sale or other disposition of property, real, personal, or mixed, acquired after February 28, 1913,

shall be the cost of such property; except that—

* * * * *

In the case of such property, acquired by gift after December 31, 1920, the basis shall be the same as that which it would have in the hands of the donor or the last preceding owner by whom it was not acquired by gift. If the facts necessary to determine such basis are unknown to the donee, the Commissioner shall, if possible, obtain such facts from such donor or last preceding owner, or any other person cognizant thereof. If the Commissioner finds it impossible to obtain such facts, the basis shall be the value of such property as found by the Commissioner as of the date or approximate date at which, according to the best information the Commissioner is able to obtain, such property was acquired by such donor or last preceding owner. * * *

Section 213 of the same Act defines "income" as follows (p. 237):

That for the purposes of this title (except as otherwise provided in section 233) the term "gross income"—

(a) Includes gains, profits, and income derived from salaries, wages, or compensation for personal service (including in the case of the President of the United States, the judges of the Supreme and inferior courts of the United States, and all other officers and employees, whether elected or appointed, of the United States, Alaska, Hawaii, or any

political subdivision thereof, or the District of Columbia, the compensation received as such), of whatever kind and in whatever form paid, or from professions, vocations, trades, businesses, commerce, or sales, or dealings in property, whether real or personal, growing out of the ownership or use of or interest in such property; also from interest, rent, dividends, securities, or the transaction of any business carried on for gain or profit, or gains or profits and income derived from any source whatever. The amount of all such items (except as provided in subdivision (e) of section 201) shall be included in the gross income for the taxable year in which received by the taxpayer, unless, under methods of accounting permitted under subdivision (b) of section 212, any such amounts are to be properly accounted for as of a different period; but

(b) Does not include the following items, which shall be exempt from taxation under this title:

* * * * *

(3) The value of property acquired by gift, bequest, devise, or descent (but the income from such property shall be included in gross income).

STATEMENT

In the *Taft case,* petitioner prior to April, 1922, and after December 31, 1920, received as gifts from her father 150 shares of common stock of the Nash Motors Company. (R. 4, 5.) These shares were originally obtained by petitioner's father as a bonus

in connection with the purchase by him of preferred stock of said company, and the amended complaint alleges that the common stock received by him at that time had no market price or value. (R. 6.) As the result of a stock dividend declared in February, 1923, petitioner became the record owner of 750 shares of common and 450 shares of preferred stock in the Nash Motors Company. Some time later, in 1923, petitioner sold 200 shares of common and 130 shares of preferred stock for $34,345.30. (R. 5.) The market value of the original 150 shares of common stock at the time the gifts were made was $42,350. By a method of allocation, as to which there is no dispute, it is found that the shares which were sold in 1923 for $34,345.30 were worth $11,-708.80 when received by petitioner from her father. (R. 6.) In making her return for 1923, petitioner, pursuant to Section 202(a)(2), *supra,* included the entire proceeds of the sale of the stock as income and paid the tax thereon under protest, taking the position that only the difference between the value of the stock when she acquired it and the price at which she sold it was taxable income within the meaning of the Sixteenth Amendment to the Constitution. Accordingly a claim for the refund of $2,040.09, representing the amount of the tax in dispute, was duly filed and after six months this action was brought for recovery. (R. 5, 7–8.)

In the *Greenway case,* petitioner prior to April, 1922, and after December 31, 1920, received as gifts from his brother 10,000 shares of the capital stock

of the Ahumada Lead Company. These shares were originally purchased by petitioner's brother for $10,000. The market value of said shares at the time the gifts were made was $30,000. Subsequently, on or about August 1, 1922, petitioner sold the said 10,000 shares of stock for $52,500. (R. 4–5.) In making his return for 1922, petitioner, pursuant to Section 202(a)(2), *supra,* included as income the sum of $42,500, which represented the difference between the cost of said shares to his brother and the price for which petitioner sold them, and paid the tax thereon under protest, contending that only the difference between the value of the stock when petitioner acquired it and the price at which he sold it was taxable under the Constitution. (R. 6–7.) Upon the rejection by the Commissioner of Internal Revenue of a claim for refund of $4,441.61, representing the amount of the tax in dispute (R. 8), this action was brought for recovery.

The District Court for the Southern District of New York sustained the position of petitioners, holding that no part of the value of a *bona fide* gift as of the date of delivery constitutes taxable income in the hands of the donee within the meaning of the Sixteenth Amendment, and that a tax upon a donee measured by the increase in value from the time the donor originally acquired it until the time the donee sold it was a direct and unconstitutional tax on the gift itself. (*Taft case,* R. 13; *Greenway case,* R. 20.)

Upon writs of error the judgments of the District Court were reversed by the Circuit Court of Appeals for the Second Circuit, each of the three judges rendering separate opinions, one dissenting. (*Taft case,* R. 27–42; *Greenway case,* R. 33–48.) The two prevailing opinions, in upholding the constitutionality of the law, reached that conclusion by somewhat different lines of reasoning.

Provisions similar to Section 202(a)(2) of the 1921 Act here involved are also to be found in Section 204(a)(2) of the Revenue Acts of 1924 and 1926, respectively, c. 234, 43 Stat. 253, 258 (U. S. C., Title 26, Sec. 935); c. 27, 44 Stat. 9, 14 (U. S. C., App., Title 26, Sec. 935). In addition, Section 204(a)(3) of each of those Acts applies the same rule to property acquired after December 31, 1920, "by a transfer in trust."

CONCLUSION

The question presented is one of first impression and of general importance. The same question is involved in a great many other cases now pending in the courts, before the Board of Tax Appeals, and before the Treasury Department. It is desirable that it be settled by this Court, and there is no reason for opposing the issuing of the writ.

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OCTOBER, 1927.

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